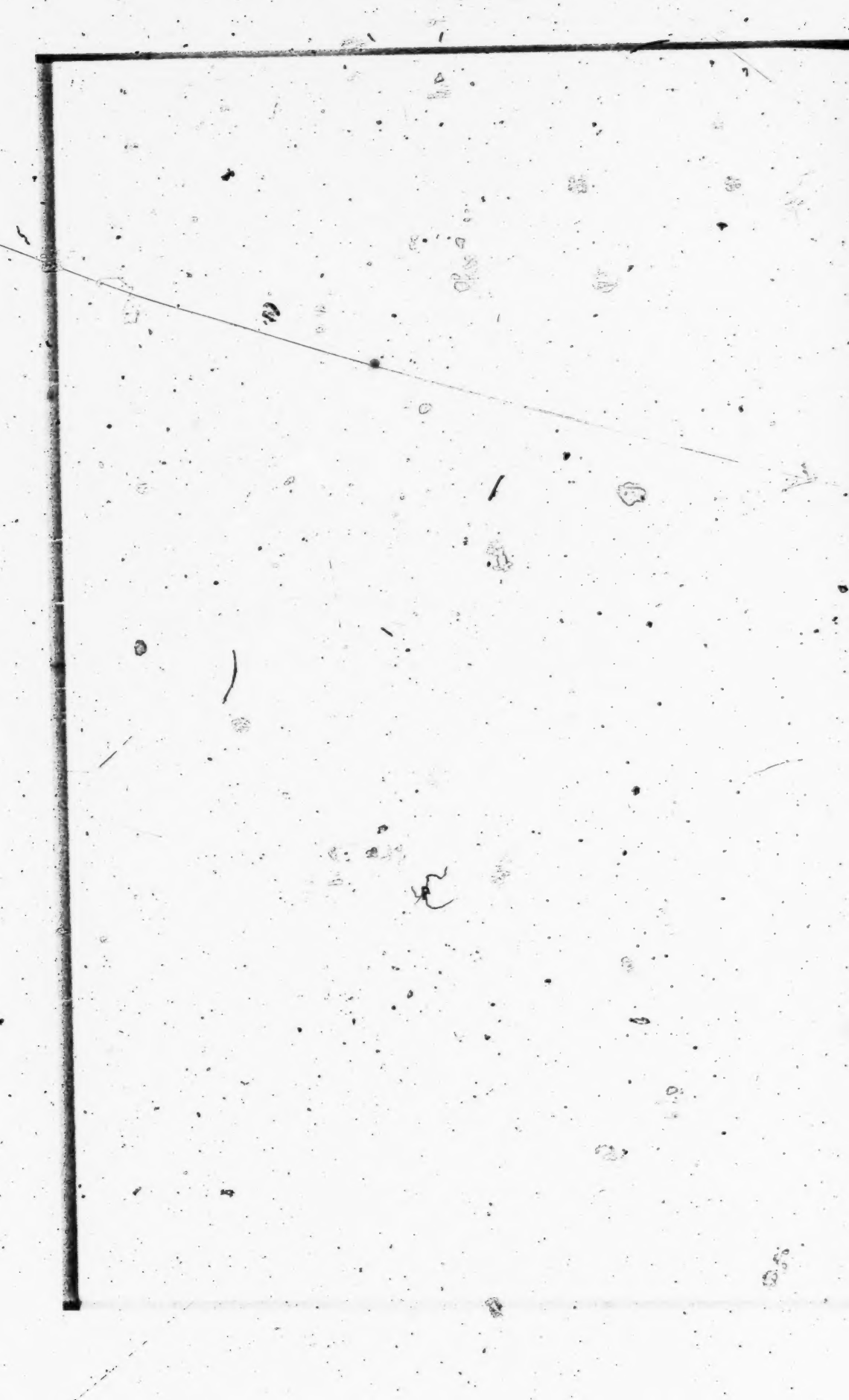

Nos. 962 - 963

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1932

No.

FIRST NATIONAL BANK OF CINCINNATI and INTERNATIONAL HEATER COMPANY,
Petitioners (Appellants Below),

against

RUDOLPH B. FLERSHEM, CHARLES O. CORNELL, JOHN H. WATERS and FRANK B. CAHN, as the Reorganization Committee constituted under the Plan and Agreement dated February 11, 1931, for the Reorganization of NATIONAL RADIATOR CORPORATION and BANKERS TRUST COMPANY, Trustee, NATIONAL RADIATOR CORPORATION (Delaware), NATIONAL RADIATOR CORPORATION (Maryland), ROBERT S. WATERS and WILLIAM G. HEINER, Receivers, CARL E. RESLEY and G. FRANKLIN LUDINGTON,
Respondents (Appellees Below).

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

RALPH ROYALL,
JAMES F. HUBBELL,
HORACE F. BAKER,
Counsel for Petitioners.

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Respondents (Appellees Below).

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

To the Honorable Charles E. Hughes, the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

First National Bank of Cincinnati and International Heater Company, the above-named petitioners, respectfully pray that a writ of certiorari issue to review the decree of the United States Circuit Court of Appeals for the Third Circuit filed on the 24th day of March, 1933, affirming the final decree of sale filed in the United States District Court for the Western District of Pennsylvania on the 31st day of May, 1932, and the decree confirming the sale and approving the Plan of Reorganization filed therein on the 8th day of September, 1932 in the Federal Equity suit brought in that Court entitled "Rudolph B. Flershem, et al, as the Reorganization Committee, etc., Complainants, against National Radiator Corporation, Defendant."

STATEMENT

This is a suit brought by the Reorganization Committee as complainants in the United States District Court for the Western District of Pennsylvania for the purpose of effectuating a plan of reorganization of National Radiator Corporation (the defendant). The suit resulted in the making of a perfunctory judicial sale in a manner studiously designed to effectuate a transfer of all of the assets of the corporation to the nominee of the Reorganization Committee for the sum of $2,500,000., although in 1927 the same interests as those sponsoring the reorganization represented the corporate assets as

having a value of approximately $25,000,000. This representation was made in connection with the sale at that time of $12,000,000. of debentures.

The petitioner First National Bank of Cincinnati is the owner of $68,000. in face amount of such debentures which were acquired by it at the time of their issue at the issue price of $1,000. a debenture.

The petitioner International Heater Company is the owner of $60,000. of corporate notes issued to it by the corporation on account of payment of the purchase price for its interest in property acquired from it by the corporation in 1928. These notes became due serially at the rate of $20,000. per annum.

The debentures were unsecured. There were no other creditors who had security. All the creditors were unsecured general creditors.

The suit had its genesis at a directors meeting of National Radiator Corporation held on the 31st day of January, 1931, at which it was resolved to default upon the debenture interest due February 1, 1931 and to ask the complainants, who include the two ranking officers of the corporation, to act as a Reorganization Committee. It was also resolved that the corporation should undertake to pay the expenses of the Reorganization Committee. (R., pp. 750-1) A Plan of Reorganization dated February 11, 1931 for the benefit of debenture holders and preferred and common stockholders was immediately promulgated. After obtaining the deposit of a large majority of the debentures and preferred and common stocks, the Committee filed this suit as complainants on October 5th, 1931. (R., p. 10) The answer of the complainants to the intervening petition of First National

Bank of Cincinnati admits "that they filed the bill of complaint in this cause as a step in effectuating the Plan and Agreement of Reorganization dated February 11, 1931." (R., p. 150) The bill of complaint prayed "that the properties and assets and business of the defendant may be ordered to be sold as an entirety." (R., p. 20) The answer of defendant National Radiator Corporation to the bill of complaint "admits the truth of the allegations therein contained, joins in the prayers thereof, and consents to the appointment of a receiver or receivers as therein prayed for." (R., p. 93) Upon the filing of this bill of complaint and this answer the Court, without legal notice to anyone, on the 9th day of October, 1931 made a decree completely sequestering the assets of the corporation in the Court's hands and appointing Robert S. Waters, the Vice President and General Manager of the corporation, and William G. Heiner as Receivers and enjoining suits. (R., pp. 95-101)

The National Radiator Corporation was organized in August 1927 to effectuate a merger of six corporations with far-flung plants located in nine states engaged in the business of manufacturing boilers, radiators and similar articles. A public issue of $12,000,000. of unsecured debentures was made in August 1927 by the respondent Bankers Trust Company as the banking house of issue for the purpose of effectuating this merger. It would perhaps be more accurate to say that the merger was for the purpose of effectuating the issue. The Bankers Trust Company is also the trustee under the indenture relating to the debentures and also served in the third capacity of depositary under the Plan of Reorganization dated February 11, 1931. The banker's cir-

cular upon which the debentures were sold in 1927, showed assets of $26,192,261.72 and liabilities of $1,478,061.72 other than the liability upon the $12,000,000. of debentures and upon preferred and common shares of stock which had a stated liability of $11,500,000. (R., pp. 405-7.)

The operations of the corporation for the full years of its operation after the merger became effective and until the receivership, that is to say, the years 1928, 1929 and 1930, showed losses after depreciation of over $1,200,000. in each of those years and aggregate losses for the three years of approximately $4,000,000. after interest on the debentures and of approximately $2,000,000. before such interest. (R., p. 209) This, although as is well known, 1928 and 1929 were banner years. The business as an entirety was a demonstrated failure.

In February, 1931 at the time the corporation defaulted on the semi-annual interest payment upon the debentures and at which time the Reorganization Committee was organized and the Plan of Reorganization, dated February 11, 1931, was promulgated, the corporation had current assets of $5,054,007.30 of which $1,701,899.94 was cash. There were then other assets sufficient to bring the total up to $19,434,548.08. The only presently payable liabilities, other than the debenture interest then about to fall due, were $46,787.60 of accounts payable. (R., pp. 51-2)

In the spring of 1932 the respondents, without notice to the creditors, submitted to the District Court the final decree of sale above referred to which was signed and filed in that Court on May 31, 1932. (R., p. 420) The three ranking officers of the corporation, Mr. John

H. Waters, President (and chief stockholder), Mr. Rudolph B. Flershem, Chairman of the Board, and Robert S. Waters, Vice President and General Manager (and the President's son), the first two of whom are also members of the Reorganization Committee, were placed upon the stand by the respondents to testify as to upset price. They wanted to buy the property as cheaply as they could. They testified that about $2,300,000 was an appropriate price. (R., pp. 232, 343) The receiver Heiner, who may be said to have been the Court's receiver, was also called by counsel for the Reorganization Committee to testify to the same effect. (R., p. 381) Both of the receivers, as well as the Reorganization Committee, were represented by the same counsel. (R., p. 120).

The decree submitted and signed provided for the sale at New Castle, Pennsylvania, of the property as an entirety, including cash, Liberty bonds, accounts receivable, receivers' inventory, plants and machinery, numerous warehouses, numerous dwellings and an office building and an apartment house situated in nine different states. A study of the provisions of the decree in this respect will show that it was studiously designed to effectuate a perfunctory judicial sale for the purpose of accomplishing the Plan rather than a real liquidation for the purpose of bringing about the best possible yield to the trust in the Court's hands. (R., pp. 445, 470, 474.)

The Court fixed $2,500,000. as the upset price for such sale.

At the time of this hearing the current assets to be the subject of this sale consisted of the following:

Cash	$852,096.29
United States Certificates of Indebtedness	980,000.00
Accrued interest thereon	6,124.97
Bank Certificates of Deposit	50,000.00
Cash surrender of Life Insurance	22,900.00
New York State Bonds	18,686.33
Accounts Receivable	858,992.41
Inventory	1,634,905.25
Total	$4,423,705.25

In addition to this, there were plants and machinery carried in the receivers' inventory after full depreciation at $6,635,842.84. In addition thereto, there were the rights as creditor, majority stockholder and equitable owner of the rest of the stock of the Steel Boiler Company. In addition there were the patents, trade-marks and trade-names which with good-will were carried by the corporation at over $6,000,000. as well as other valuable items. (R., pp. 381-382)

The Court took no measures at all to assure itself that the sale conducted under such decree and at such an upset price would yield as much as would the holding in the hands of the receivers of the cash, Liberty bonds and receivables and the careful and business-like sale of the inventory and machinery and plant equipment and of the very numerous pieces of real estate in separate lots and the taking of appropriate steps to effectuate a recovery and liquidation of other assets hereafter mentioned. The Court did not secure an appraisal and acted only upon the so-called opinion of the purchasers who wanted to buy the property as cheaply as they could.

The petitioner First National Bank of Cincinnati, which at the time of the hearing was making an application to intervene (R., p. 3), became apprised of the application for the final decree of sale and was permitted to cross-examine the above-mentioned witnesses. This party besought the Court to take suitable measures in order to investigate the value of the properties and the best method of realizing upon the fund for the protection of this intervenor and of each and every other creditor of the trust fund in the hands of the Court, but this the Court refused to do.

The petitioner International Heater Company was not heard at all upon the application for the decree of sale and learned only by chance of the decree after it had been signed. It thereafter intervened (R., p. 200) and, together with the petitioner First National Bank of Cincinnati appealed to the Circuit Court of Appeals from the final decree of sale dated May 31, 1932 (R., p. 490) These petitioners also joined in contesting the propriety of making the further decree dated the 8th day of September, 1932, approving the Plan and directing the transfer of the assets (the trust fund) from the custody of the Court to the new corporation, and joined in appealing from that decree. (R., p. 712)

The Reorganization Committee (complainants) acted on behalf of debenture holders, preferred stockholders and common stockholders. The Plan provided that the rights of the debenture holders as creditors should be cut in half and that their right to receive interest should depend upon earnings. At the same time, the Plan preserved in the preferred stockholders a substantial share in the assets of the corporation without imposing any

condition by way of contribution of new capital, or otherwise; in other words, gave them a "free ride." The Plan also provided that the common stockholders, upon the payment of the nominal sum of One dollar in respect to each three shares of old common stock, might acquire a warrant evidencing their right to buy stock of the new corporation at a fixed price at any time within the next ensuing twenty years. (R., p. 61) The Plan also provided that the Committee should have the discretion to pay certain ordinary creditors in full in cash (R., pp. 65-6); and, in carrying out the Plan, all the miscellaneous general creditors were paid in full in cash. (R., p. 648-9)

As to these petitioners, however, they were permitted to receive only the securities of the new corporation as arranged by the Committee or be relegated to the receipt of such dividend as would follow from such upset price as the complainants might be able to induce the Court to fix after the deduction therefrom of the amount of such allowances to the complainants and the receivers and the Trustee and their respective counsel as the Court might be induced to grant. (R., pp. 456-458) The decree contains a provision reserving out of the cash included in the sale the sum of $300,000. to be used for such and similar purposes. (R., p. 453)

In 1927 the respondents represented the assets to be worth $25,000,000. In 1931 they carried them at $19,000,000. In 1932 they passed them through the Court to their new corporation with a capital structure of $16,000,000. (R., p. 56, 58-60) But while the assets constituted a trust in the Court's hands, they said they were worth but $2,500,000. The Courts

below adopted their views. What is there in the judicial touch which renders assets comparatively valueless when constituting a trust although of great value at every other moment?

One of these petitioners brought out upon the cross-examination of respondents' witnesses that there had been developed in laboratories of the corporation, by officers and employees of the corporation, and at the expense of the corporation, a new type of steel boiler, and that the capital for financing the manufacture and sale of these special boilers was also furnished by the corporation; also, that the patents and devices were put into another corporation called the "National Steel Boiler Company," but that only a bare majority of this stock was issued to defendant corporation, the rest of it being issued to some of its officers and employees who claim to own it in their individual rights. (R., pp. 299-303) As to this new invention, it was stated in a printed circular addressed by the Reorganization Committee to the debenture holders that the corporation "has developed new and improved products of great promise including, among others, steel boilers." (Record, pp. 529-530) That petitioner besought the Court to take appropriate action to have this transaction, which on its face seemed fraudulent, undone in order that this apparently valuable asset might be recovered for the benefit of the creditors. The Court below, as well as the Circuit Court of Appeals, refused to make any such provision but decreed a sale of all the assets as an entirety to the nominee of the Reorganization Committee with the result that the old interests have acquired the rights of the corporation and have thus been put in a position to

give themselves immunity for their seemingly fraudulent acts in this important transaction.

The further result of the decrees is to continue the business in the hands of the same management under whose charge it was a demonstrated failure.

Upon the joint appeal to the Circuit Court of Appeals by these petitioners from these decrees of the United States District Court of the Western District of Pennsylvania the Circuit Court of Appeals of the Third Circuit made a decision dated the 24th day of March, 1933 affirming them.

In the opinion handed down by the District Court and in the opinion also handed down by the Circuit Court of Appeals, both Courts refrained from discussing the main point urged before each of such Courts by these petitioners, that, the Court having sequestered the whole of the debtor's property for the protection of creditors and enjoined suit, the fund constituted a trust in the hands of the Court, and that each and every creditor had a fundamental right to the due administration by the Court of such trust in such manner as to provide the greatest possible payment to each of the creditors.

THE QUESTIONS PRESENTED:

(1) Did not the District Court, having sequestered all of the assets of National Radiator Corporation in its hands and having prohibited by injunction all creditors from pursuing their legal rights, become charged with a trust to fairly and duly administer the fund for the benefit of each and every creditor, or, in other words, did not the Court become a "judicial trustee" of the fund thus sequestered in its hands?

(2) Did not such Court owe the duty to each and every creditor to see to it that the fund was administered in such manner as to effect a recovery and liquidation of the assets of the debtor corporation so as to provide the greatest possible payment to the creditors and to each and every one of them?

(3) Did not the Court violate the rights of these petitioners in signing the final decree of sale dated May 31, 1932 proposed by the Reorganization Committee, with provisions studiously designed to bring about merely a transfer of the corporate assets to them for the purpose of effectuating the Plan of Reorganization and with an upset price of $2,500,000. for all of the assets of this corporation, without investigation by the Court as to the best means of liquidating such assets so as to produce the greatest possible yield to each and every creditor, and acting without inventory or appraisal, and merely upon the suggestion of the purchasers as to the price at which they should be permitted to acquire the trust assets.

(4) May a Federal court of equity in such a proceeding properly make a decree of sale for the purpose of effectuating a Plan of Reorganization which reduces the rights of the creditors as such in the assets of the corporation, while preserving an interest for its preferred stockholders without the requirement of a contribution of new capital by such stockholders as the condition of the preservation of such interest?

(5) May a Federal court of equity in such a proceeding properly decree a sale of all the corporate assets for the purpose of effectuating a Plan of Reorganiza-

tion under which some of the general creditors are paid in full in cash out of the assets of the corporation, while others are relegated to a dividend based upon an upset price fixed by the Court to yield approximately 15c to 20c on the dollar?

(6) May a Federal court of equity in such a proceeding decree the assets to be sold as an entirety, including the rights of the creditors growing out of a seemingly fraudulent diversion of the assets of the corporation by those in control to themselves, without investigation by the Court as to the value of the assets so diverted, or without provision for the recovery thereof upon behalf of the creditors and with the result that the purchasers are thus put in a position to give themselves immunity for their seemingly fraudulent and illegal acts in having diverted important assets of the corporation for their own benefit?

(7) Did not the District Court exceed its jurisdiction and power in making the decree, dated September 6, 1932, directing the transfer from the custody of the Court to the new corporation of the corporate assets (the trust fund) ordered to be sold under the final decree of sale, dated May 31, 1932, these petitioners having theretofore taken and perfected their appeal to the Circuit Court of Appeals from such final decree of sale, dated May 31, 1932?

REASONS FOR THE ALLOWANCE OF THE WRIT

(1) The Courts below violated their trust obligations to these petitioners and to the other creditors of the de-

fendant corporation which obligation arose from the sequestration by the Court in its hands of all the corporate assets and the enjoining of the exercise by the petitioners and the other creditors of their legal remedies; the Courts below thus impaired the petitioners' contracts and, in effect, confiscated their vested legal rights; the proceedings below were a clear departure from the accepted and usual course of legal procedure.

(2) The Courts below, in decreeing a sale of the corporate assets as an entirety for the purpose of effectuating the Plan of Reorganization and in approving the plan and effectuating it, violated the fixed principle established by the decisions of the United States Supreme Court in numerous cases including the case of *Louisville Trust Company v. Louisville N.A. & C.R. Co.*, 174 U. S. 674, 43 L. Ed. 1130 (1899) in that the subordinate rights of the stockholders were here secured at the expense of the prior rights of the creditors including these petitioners; and also violated other principles which manifestly should govern in such matters in that the plan was designed to effectuate and did result in the payment in full in cash of some creditors of the same class and of equal rank with the petitioners while allowing to the petitioners only the receipt of certain securities of comparatively small value.

(3) The District Court in directing the delivery of all of the assets of the corporation to the nominee of the Reorganization Committee pending the decision of the appeal from the final decree of sale, which appeal had been previously taken and perfected, acted beyond its jurisdiction and power and in violation of the rule laid down by this Court in the case of *Hovey* v. *McDonald*,

109 U. S. 150, 27 L. Ed. 888 (1883) and since recognized in numerous decisions.

THE IMPORTANCE OF THE QUESTIONS

This Court has recently in its decisions in *Shapiro* v. *Wilgus*, 77 L. Ed. 149 (December, 1932); *Michigan* v. *Michigan Trust Co.*, 286 U. S. 334, 76 L. Ed. 1136 (1932) and *Harkin* v. *Brundage*, 276 U. S. 36, 72 L. Ed. 457 (1928); issued distinct warnings in respect to the conduct by the Federal courts in proceedings of this nature in which consent sequestration decrees are obtained in Federal equity suits in order to effectuate a reorganization of ordinary industrial corporations and to bring about judicial coercion of creditors who are not willing to accept the wishes of the stockholders or managers of the corporation or other proponents of such plans.

The prevalence of such proceedings and the manner in which they have been conducted by the Federal courts is presently the occasion of much public comment and criticism.

The courts below in this proceeding, as well as other Federal courts in other similar proceedings, have shown a tendency to depart from the accepted and usual course of judicial proceedings in that they have allowed themselves to be employed in proceedings designed to bring about the destruction of legal rights rather than the upholding and enforcement thereof, which is and should be their fundamental purpose.

It is especially important in view of the existing financial condition and the many failures of corporations

of this type that this Court should clearly define the powers and duties of Federal judges in the conducting of proceedings of this nature.

WHEREFORE, it is respectfully submitted that this petition for a *writ of certiorari* to review the decree of the Circuit Court of Appeals of the Third Circuit dated the 24th day of March, 1933 and the decrees of the United States District Court for the Western District of Pennsylvania dated respectively the 31st day of May, 1932 and the 8th day of September, 1932 which were affirmed by the decree of the Circuit Court of Appeals should be granted.

FIRST NATIONAL BANK OF CINCINNATI and
INTERNATIONAL HEATER COMPANY

by

RALPH ROYALL,
JAMES F. HUBBELL,
HORACE F. BAKER,
Counsel for Petitioners.

BRIEF IN SUPPORT OF PETITION

OPINIONS OF THE COURTS BELOW

Neither the opinion of the Circuit Court of Appeals of the Third District nor the opinions of Judge Gibson in the District Court are yet reported. The opinions of Judge Gibson are printed at page 416 and page 691 of the record. Printed copies of the opinion of the Circuit Court of Appeals are filed herewith.

JURISDICTION

The jurisdiction to issue the writ is found in Section 240a of the Judicial Code as amended by the Act of February 13, 1925, c. 229, Sect. 1, 43 Stat. 938; Sect. 347a of Title 28, U. S. C.

STATEMENT OF FACTS

The statement set out in the foregoing petition is here adopted but may be supplemented by the following matter.

Since the District Court and the Circuit Court both put great stress upon the fact that the Reorganization Committee was seeking to save the business and that about 95% of the debenture holders had deposited their debentures with the Committee and thus assented to the plan, it becomes material to state how this large representation was brought about.

When publicly owned securities in a corporation such as this are defaulted, the individual security holder has

little choice of action. A reorganization plan proposed by the management and sponsored by the banking house of issue is adhered to generally as a matter of pure inertia. The plan is accepted by the rank and file for the simple reason that they have no other practical recourse or remedy.

In the instant case it is true that the debenture holders were given an opportunity to rally in protection of their interests under the standard of an opposition Protective Committee, but as soon as this movement gained strength the proponents of the plan were able to arrest it by inducing the "Protective Committee" to abandon their opposition, and thus the last practical opportunity for the ordinary debenture holders to make any choice was removed. The Reorganization Committee whose expenses, as above stated, were underwritten by the corporation, agreed to pay the opposition "Protective Committee" $35,000 for services etc. in return for the "Protective Committee" turning over to it nearly $1,000,000 of debentures which had been deposited with the so-called "Protective Committee" and abandoning their opposition. (R., p. 759) Lip service was paid to the request of the "Protective Committee" that changes in the plan be made, but these changes were immaterial and without substance. (R., pp. 537-40, 568-74).

Nor should the judgment of the sponsors of such a plan of reorganization be regarded as conclusive under the circumstances. This is so for the reason that they are prejudiced. The plan of reorganization here was sponsored by those who sponsored the merger,—that is to say, the officers of the corporation and Bankers Trust Company, which acted as the banking house of issue of

the $12,000,000 of debentures. Human nature being what it is, their reluctance to admit error in having brought about this ill-conceived merger would induce them to sponsor this ill-conceived reorganization, even if that were not the best thing to be done in the real interests of the creditors. The management is further prejudiced because while the business goes on they will continue to enjoy their salaries.

The conviction of these petitioners, First National Bank of Cincinnati, and International Heater Company, is that the fact of huge deficits for the whole history of the corporation, even including the excellent industrial years of 1928 and 1929, establishes that the merger was ill-conceived and that, by the same token, the reorganization is ill-conceived and against the interests of the creditors. This is the only conclusion consistent with the facts.

In the broad aspect of the matter, one of the fundamental errors arises from the gratuitous assumption by the Courts below that it is a constructive and a beneficial thing for the corporation to be reorganized. We do not believe Courts should proceed upon such gratuitous assumptions. Where, as here, the business of an ordinary industrial corporation is a demonstrated failure, plans for reorganization are not constructive or of a beneficial nature for the creditors or in a broader economic sense. We submit it is better that, when such a business is a demonstrated failure, as much as possible of the creditors' money should be gotten out. We submit further that any other course violates the creditors' fundamental legal right.

We believe that this fundamental error of the Courts below in this case is evidenced in other frequent instances and that Federal Equity Courts are too prone to assume in almost every sort of situation that a reorganization plan for a failed industrial corporation is a constructive and a beneficial thing. We also believe that there is a clear tendency in the lower Federal Courts to permit themselves to be used as a means of coercion in proceedings brought for the purpose of effectuating such plans and that this is clearly against all proper conceptions of the usual and accepted course and purpose of judicial proceedings.

The opinions of both the Courts below show clearly that these Courts were laboring under a further fundamental error in that they determined the matter as though it were the trial of issues in an ordinary law suit between these petitioners on the one side and the complainants, the corporation and the Bankers Trust Company, as Trustee, on the other. The Courts below put much reliance upon the fact that the Reorganization Committee offered themselves as witnesses to give their opinion as to the appropriate upset price at which they should be permitted to buy the property, and that, as these petitioners did not offer witnesses to testify otherwise, the matter must be disposed of as though an issue were presented for adjudication upon uncontroverted testimony. **This means that these two creditors, who are beneficiaries of the trust fund and who were beseeching the Court to perform its trust duty to them and to the other creditors, must, at their own expense, call experts to come forward with appraisals of elab-**

orate plants and plant equipment located in nine different states, as well as experts with opinions upon the value of other property. The expense of such an undertaking might well exceed the face value of the claims of either one of these objecting creditors, even though their claims are of comparatively large amounts. No holder of relatively few debentures could afford to undertake the burden and expense of thus protecting the trust fund in the interest of all the other debenture holders. In any case, it is not their duty but the duty of the Court, the judicial trustee.

Furthermore, it was here manifest that, in view of the nature and amount of the assets constituting it, as to which the evidence was undisputed, the trust fund could have been made to yield by ordinary and careful methods of liquidation an amount largely in excess of the $2,500,000 upset price fixed by the Court. The prejudiced testimony of those seeking to acquire the trust property for a small price did not overcome these undisputed figures.

The fund is in the hands of the Court for administration as a trust. As above stated, the decree indicates that the Court has in mind the use of the fund to the extent of perhaps as much as $300,000 for administration allowances. The decree shows that the Court has in contemplation the making of these allowances to the Reorganization Committee, the Receivers, and the Bankers Trust Company, as Trustee, and their respective counsel (R., p. 456, 457),—all of whom were seeking, not to defend the trust, but to defeat it by having the Court turn over the assets to their nominee at as low a price

as they could induce the Court to fix. The Courts have proceeded thus far in the case upon the basis that several hundred thousands of dollars of the fund may be made available for allowances, etc., for those who stand in the position of seeking to defeat the trust and the rights of the trust beneficiaries, while any of the trust beneficiaries who seek from the Court a true administration of the trust fund are told that, if the fund is to be protected, this must be done at their individual expense.

SPECIFICATION OF ERRORS

I. The Courts below erred in not carrying out under the Court's supervision a liquidation by separate sales properly designed to bring about the best yield from all the various far flung properties, reserving in the Court's hands the cash and Liberty Bonds and receivables and other virtually liquid assets; and in granting in lieu thereof the desire of a group of the creditors and stockholders that the property be turned over to them as an entirety, without taking such steps and making such investigations as would show beyond peradventure that in so doing the Court did not in effect violate its trust duties or the rights of any of the creditor beneficiaries.

2. The Courts below erred in approving the plan in that it failed to give full recognition to the rights of creditors while reserving in the stockholders an interest in the assets of the corporation; and in that the plan provided for discrimination between general creditors of the same class by paying some of them in full in cash

while only providing for others securities in the new corporation of comparatively little value.

3. The District Court erred in parting with the trust fund and directing the delivery of it to the new corporation, there to be consumed and wasted, after the appeal from the final decree of sale had been perfected, as the Court then had become powerless further to act in the premises.

ARGUMENT

I

As said by this Court in *Hollins* v. *Brierfield Coal & Iron Company,* 150 U. S. 371, 37 L. Ed. 1113 (1893) at page 383, in speaking of corporate assets sequestered in the hands of Receivers in a Federal equity suit of this nature,

> "It is * * * a trust in the administration of the assets after possession by a court of equity * * *."

The proposition would seem axiomatic. **It manifestly follows that the Court, having sequestered in its hands the assets of the corporation for the purpose of administering them as a trust for the benefit of creditors, is under a clear duty to do just that thing.**

Even though the Court might, as here, with propriety proceed to a final decree of sale of such assets as an entirety without prior notice to the creditors of the application for the making of such decree, which is doubtful, it would follow all the more that in so doing

the Court should be most mindful of its trust duties to each and every creditor beneficiary and see to it that such steps were taken as should satisfy a court beyond peradventure that in so doing it was not in practical effect violating the rights of any creditor beneficiary. This, the Court below clearly failed to do.

It is not sufficient to justify the course adopted for the Court to say, as the opinions of the District Court and the Circuit Court of Appeals seem to hold, that it was done at the behest of 95% of the creditors. This is not a corporate election. It is the judicial administration of a trust. A majority of the beneficiaries of a trust may not induce a breach of trust.

II

The plan clearly violates the "fixed principle" long ago set down by this Court and adhered to as controlling in such matters and for that reason the Courts below erred in approving the plan and decreeing a sale for the purpose of effectuating it. As said by this Court in *Louisville Trust Company* v. *Louisville N. A. & C. R. Co.*, 174 U. S. 674, 43 L. Ed. 1130 (1899), at page 684:

> "Any arrangement of the parties by which the subordinate rights and interests of the stockholders are attempted to be secured at the expense of the prior rights of either class of creditors comes within judicial denunciation."

This Court said in the case of *Northern Pacific R. R. Co.* v. *Boyd*, 228 U. S. 482, 57 L. Ed. 931 (1912) at page 504:

> "They (the stockholders) were in the position of insolvent debtors who could not reserve an interest as against creditors."

And, again, this Court in the case of *Kansas City Term. R. R. Co.* v. *Central Union Trust Company,* 271 U. S. 445, 70 L. Ed. 1028 (1926), referring to these earlier decisions, said at page 454 that this doctrine is "the fixed principle * * * and to it there should be rigid adherence".

The plan also violated the basic rights of creditors in that it discriminated between them by providing for the payment of some general creditors in full in cash while relegating other general creditors including these petitioners to the mere right to receive a diminished amount of securities of the new corporation. The attempt below to defend this arrangement as coming within the six months' rule was clearly baseless, as this rule has application only to public utility corporations and is not applicable in any sense to mere industrial corporations.

Spencer v. *Taylor Creek Ditch Co.,* 194 Fed. 635, (C. C. A. 9th 1912).

III

The authorities clearly hold that after the taking and perfecting of an appeal from the decree of a District Court, that Court is powerless to proceed further pending the appeal.

Midland Terminal Ry. Co. v. *Warinner,* 294 Fed. 185, C. C. A., Eighth Cir. (1923);
Hovey v. *McDonald,* 109 U. S. 150, 27 L. Ed. 888 (1883);

Newton v. *Consolidated Gas Co.*, 258 U. S. 165, 66 L. Ed. 538 (1921);
Merrimack River Sav. Bank v. *Clay Centre*, 219 U. S. 527, 55 L. Ed. 320 (1910).

Notwithstanding the fact that the appeal had been perfected from the final decree of sale, dated May 31, 1932, the District Court persisted, over the protest of these petitioners, in making a further decree, dated September 6, 1932, directing the delivery of the deeds to the new corporation as a nominee of the Reorganization Committee, thus permitting the trust fund to pass out of the hands of the Court and to become consumed or wasted by the new corporation. As a result of the autocratic proceedings of the District Court terminating in the final act above referred to, a position has been created which the Circuit Court of Appeals seems to have regarded as a *fait accompli* and which seems to have affected their conclusion to affirm the decrees appealed from.

CONCLUSION

It is submitted that, for the reasons above stated, a definition by this Court of the powers and duties of Federal Courts of Equity in such proceedings is most important. This proceeding has resulted in the impairment of these petitioners' contracts and in a virtual confiscation of their vested legal rights. The steps taken by the District Court in arriving at the decrees appealed from were a clear departure from the accepted and usual course of judicial procedure. The authoritative settlement by this Court of these questions at this time is

urgent in view of the prevalence of proceedings of this nature in the Federal Equity Courts.

Respectfully submitted,

RALPH ROYALL,
JAMES F. HUBBELL,
HORACE F. BAKER,
Of Counsel.